BRIEF IN SUPPORT OF PETITION HEREIN

For the sake of brevity the facts involved in the instant case will not be repeated. There is no substantial dispute concerning the same and they have been outlined in detail in the foregoing petition. The interpretation to be placed upon the terms and provisions of Sections 161 and 167 of the Revenue Act of 1932 is the only issue in the case. Said sections of the revenue statute appear in Appendix A attached to this brief.

In order that the confusion and conflict in the various decisions by the lower courts may be clearly portrayed it might be well to traverse the rocky road of decisions, reversals, contrary interpretations upon the same decisions, etc., which have taken place within the past few years in the course of an effort by various tribunals to lay down the correct rule of interpretation to be placed upon Section 167 of the Revenue Act of 1932 and the corresponding sections of prior and later revenue acts.

It might be well for the purpose of clarification to comment upon the statutes here involved, Section 161 and Section 167 of the Revenue Act of 1932 (Appendix, *infra*), since although our primary concern is with Section 167 that section cannot be properly interpreted without reference to Section 161 of which it is expressly made a part.

Section 161 declares all trust income taxable and enumerates four general categories. The first category—contained in subsection (a) (1)—may be generally described as income which the trustee has no discretion to distribute currently, but must, by reason of the restrictions of the trust itself (not merely the normal process of distribution of decedent's estate), hold until some specified time or event in the future. These characteristics distinguish this income from the three other categories mentioned in subsections (a) (2), (3) and (4). Subsection (a) (1) is

further subdivided and covers the whole field of contingent distribution.

Congress also enacted Section 167 as an exception to the general concept of the taxability of trust income announced and analyzed in Section 161. Section 167(a) (1) applies only to the last clause of Section 161(a) (1) and that clause is limited to accumulated income in which the distributee has a vested interest. The pertinent part of Section 167, here involved, taxes to the settlor of a trust (a) income which is held or accumulated for future distribution to him; (b) income which may in his discretion or in the discretion of any person not having a substantial adverse interest in the disposition of such part of the income, be held or accumulated for future distribution to him; and (c) income which may in his discretion or in the discretion of any person not having a substantial adverse interest in the disposition of such part of the income be distributed to him. The term "in the discretion of the grantor" is described in the statute (Section 167(b)) as meaning "in the discretion of the grantor either alone or in conjunction with any person not having a substantial adverse interest in the disposition of the part of the income in question." For a further and more detailed analysis of the relationship between Sections 161 and 167 of the Revenue Act of 1932, reference is made to the decision by the Federal District Court of the Eastern District of Pennsylvania in the case of *Kent vs. Rothensies, Collector*, decided on September 25, 1940, 31 F. Supp. 291.

The two problems of federal income taxation which perhaps have occasioned the most difficulty to lower courts when the issue has been applicability of the provisions of Section 167 of the Revenue Act of 1932 or comparable sections of the other revenue acts, are as follows:

1. The taxability to the grantor of the income of those trusts where the trust instrument provides for a possibility

of a reverter to the grantor time upon a contingency over which the grantor has no control, such as for example, where the instrument provides for a reverter to the grantor if the life tenant should die prior to the death of the grantor; and

2. The taxability to the grantor of the income of those trusts where the trust instrument provides for a power of amendment, alteration or termination of the trust by the grantor in the event of a contingency over which the grantor has no control, such as for example where the instrument provides that the grantor shall have the power to amend, alter or terminate the trust in the event the beneficiary predeceases him.

One of the first cases decided by the courts and having to do with the problem of applying a section of the 1924 Revenue Act (Section 219(h)), which is substantially the same as that part of Section 167 of the Revenue Act of 1932 here involved, is the case of *Kaplan vs. Commissioner*, 66 F. 2d 401. In that case it appeared that the trust instrument there under consideration named the settlor as trustee and provided in substance that the income was payable to the settlor's wife for life with reversion to the settlor if he outlived her and if he did not then to his children. The declaration also permitted the trustee to accumulate "a reasonable portion of the income," such accumulation to be payable at the discretion of the trustee to the person or persons who at the time of payment were entitled to the income of the trust. The Commissioner held that all the income of said trusts was taxable to the settlor and the Board of Tax Appeals affirmed the Commissioner.

The reviewing court modified the decision of the Board but held that since the settlor named himself trustee the large discretion given to him with respect to the accumulation of income and distribution thereof brought the trust squarely within the provisions of the statute (Section

219(h) of the Revenue Act of 1924) which was an exception to the general rule with respect to the taxability of trust income.

In applying the statute (Section 219(h) of the Revenue Act of 1924) the court said:

> "It (the statute) deals with amounts which rest 'in the discretion of the grantor,' etc.; and it operates only on 'such part of the income of the trust' as lies within that discretion."

Here was a clear case where the exception to the general rule applied since the settlor by virtue of the appointment of himself as trustee reserved unto himself a discretion with respect to the accumulation and distribution of income. Unfortunately, however, the reviewing court in the *Kaplan* case, *supra,* indulged in a bit of *obiter dictum* and in speaking again of the interpretation to be placed upon the statute, said:

> "We think the statute means that if under any circumstances or contingencies any part of the accumulated income might inure to the benefit of the grantor, such part of the income is taxable to him."

It is this *obiter dictum* which we respectfully submit has occasioned much of the difficulty and confusion in the later decisions. In this *obiter dictum* the Circuit Court of Appeals for the Second Circuit attempted to broaden the terms of the statute so that they would encompass many more situations than provided for by the statute. As the court correctly stated elsewhere in its opinion the statute deals only with amounts, the accumulation or distribution of which rests in the discretion of the grantor. That we submit is a correct and much narrower application of the statute than to say that it applies when "under any circumstances or contingencies" the accumulated income might inure to the benefit of the grantor. It was upon what we here contend was *obiter dictum* in the *Kaplan* case,

supra, that the reviewing court in the instant case decided against the taxpayer.

After the *Kaplan* case, which was decided on July 24, 1933, there reached the United States Supreme Court the cases of *Helvering vs. St. Louis Union Trust Company*, 296 U. S. 29, and *Becker vs. St. Louis Union Trust Company*, 296 U. S. 48, which involved federal estate taxes and in the decision (November 11, 1935) it was held that a "mere possibility of reverter" was insufficient to require the inclusion in the decedent's estate of property conveyed in trust by decedent in his lifetime.

The Circuit Court of Appeals for the Second Circuit in the case of *Commissioner vs. Waterbury*, 97 F. 2d 383, *certiorari* denied 305 U. S. 638 (June 6, 1938), had for consideration the taxability to the settlor of a trust where, although the income was currently distributable to the named beneficiaries, the settlor could under certain conditions and contingencies amend, revoke or terminate the trust. The only issue in the case was the taxability to the settlor of the income of said trusts under Section 167 of the Revenue Act of 1928. The court held that Section 167 did not apply to such a situation and while the decision rendered by the Circuit Court of Appeals for the First Circuit in the *Kaplan* case, *supra*, was not specifically referred to, the reviewing court in the *Waterbury* case, *supra*, reached a conclusion that was exactly contrary to what we have hereinbefore contended was *obiter dictum* in the *Kaplan* case, *supra*. In that connection the court said:

> "The phrase 'in the discretion of the grantor of the trust' we have held to be 'expressly limited to situations where the distribution or accumulation may be for the benefit of the grantor or not as he alone or in conjunction with anyone not a beneficiary may in his discretion determine.' If the distribution to the grantor with accumulation for future distribution to him occurs without the existence of

any discretionary control by the grantor, Section 167 does not apply.

It is erroneous to assume that because the grantors could acquire the trust property through the exercise of the powers of revocation in future years any income presently retained by the trustee could be taxed under Section 167. At all times during 1929 the taxable gains were not the property of the respondents but were the property of the trust."

Here, therefore, we have direct conflict between the Second Circuit, the First Circuit and the Sixth Circuit with respect to the meaning and interpretation to be placed upon Section 167 of the Revenue Act of 1932 and comparable sections of other revenue acts.

The United States Board of Tax Appeals in several decisions (*William E. Boeing vs. Commissioner*, 37 B. T. A. 178; *Moore vs. Commissioner*, 39 B. T. A. 808, and *Pyeatt vs. Commissioner*, 39 B. T. A. 774) determined that the *St. Louis Union Trust Company* cases, *supra*, narrowed that part of the *Kaplan* decision which we have heretofore in this brief contended was *obiter dictum* by the court deciding that case. Respondent acquiesced in the decisions rendered by the United States Board of Tax Appeals in the *Boeing*, *Moore* and *Pyeatt* cases. (Internal Revenue Bulletins, June 6, 1939, page 1; July 17, 1939, page 1; August 21, 1939, page 1.) Those decisions by the United States Board of Tax Appeals in substance held that the income of a trust is not taxable to the settlor thereof when under the terms of the trust both the accumulated income and the corpus of the trust might revert to the settlor in the event a beneficiary of the trust predeceased the settlor.

On June 6, 1939, the Circuit Court of Appeals for the Sixth Circuit rendered its decision in the case of *Corning vs. Commissioner*, 104 F. 2d 329. In that case federal income taxes for the year 1934 were involved. The issue concerned the taxability to the trustor of the income of a trust.

In the indenture it was provided that the income of the trust during the settlor's life was to be accumulated and added to the corpus and that after the death of the settlor's father the settlor might terminate the trust but such power to so terminate the trust could not be exercised in any event prior to 1937. The reviewing court reversed the Board of Tax Appeals and determined that Section 167 did not apply since the right reserved by the settlor to direct the return to him of the corpus of the trust was contingent upon the death of the petitioner's father during his (the settlor's) lifetime and that thus the petitioner's power to revest himself with the corpus of the trust was subject to a contingency "which might never arise." In that connection the court said:

> "It (the Board of Tax Appeals) draws a distinction between the existence of a power to revoke and the right to exercise that power. Even though the right to exercise the power to revoke may be contingent it says, nevertheless, the existence of the power during the tax year is not contingent.
>
> The distinction is difficult to apprehend. It is not consonant with generally accepted concepts of power, for a power which is not presently exercisable and may never be capable of being exercised does not exist. 1 Sugden on Powers, 3d Amer. Ed. 371, 372. It is difficult, therefore, to comprehend that one may be vested with a power that is not presently nor with certainty exercisable *in futuro*.
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> * * * It does not follow from this, however, that the Congress in the 1934 Act used either the term 'power' or the term 'vested' in a sense other than these terms were used in the 1928 or preceding Revenue Acts, and the committee reports of the Congress do not so indicate. The term 'power' as used in corresponding sections of earlier acts has not been thought to extend to the reservation of a right conditioned upon a contingency that may never occur. *Commissioner vs. Stokes*, 3d Circuit, 79 F. 2d 256; *Higgins vs. White*, 1st Circuit, 93 F. 2d 357."

In the *Corning* case, *supra,* the Sixth Circuit had for its consideration a situation which differed from those considered by the United States Supreme Court in the *St. Louis Union Trust Company* cases, *supra,* and by the United States Board of Tax Appeals in the *Boeing, Moore* and *Pyeatt* cases, *supra.* In those cases the trust instruments provided for a reversion timed upon a contingency, whereas in the *Corning* case, *supra,* and in the *Waterbury* case, *supra,* the revestment in the grantor could not take place until a power was exercised by the settlor which the Sixth Circuit Court of Appeals in the *Corning* case said would not exist until the contingency upon which it was timed arose. In the instant case the power in the settlor alone to alter, amend or terminate the trust arises only upon the prior decease of his wife, Mary Kaufman Altmaier, and therefore it was asserted by the petitioner here that the rule laid down by the Second Circuit in the *Waterbury* case and by the Sixth Circuit in the *Corning* case controlled and consequently the provisions of Section 167 did not apply.

Then came the decision by this court in the case of *Helvering vs. Hallock,* 309 U. S. 106, which involved federal estate taxes and which specifically reversed the decisions by this court in the *St. Louis Union Trust Company* cases, *supra.* Other cases were considered by the Supreme Court with *Helvering vs. Hallock, supra, Rothensies vs. Huston, and Bryant vs. Helvering.* In all the cases considered, however, the trust agreements provided for a reverter to the settlor upon the prior death of the life tenant but if the life tenant outlived the settlor then the *corpus* was to go in the *Hallock* case to the settlor's children, in the *Huston* case to the life tenant in fee, and in the *Bryant* case to the estate of the settlor upon the death of the life tenant. This court held that in each instance the *corpus* of the trust was to be included in the settlor's gross estate for federal estate tax purposes, relying upon the rule laid

down in the case of *Klein vs. United States*, 283 U. S. 231. In the *Klein* case this court had held that there should be included in the gross estate of a grantor of a trust the *corpus* of the trust, where the decedent had during his lifetime conveyed land to his wife for her lifetime with reversion in fee vested in the decedent grantor if his wife predeceased him.

Thus is appears that in the *St. Louis Union Trust Company* cases, in the *Klein* case, in the *Hallock* case and in the *Boeing, Moore* and *Pyeatt* cases, decided by the United States Board of Tax Appeals (all *supra*) the trust instruments in each instance provided for a reverter to the settlor timed upon a contingency. None of those cases involved a trust where the settlor had a right timed upon a contingency over which he had no control to alter, amend or terminate the trust. The *Waterbury* and the *Corning* cases, *supra*, involved such a situation and the courts in those cases held that Section 167 of the Revenue Act of 1932 or comparable sections of other Revenue Acts did not apply, the Sixth Circuit in the *Corning* case specifically stating that such a power did not in fact exist until the contingency arose.

That this is not a distinction without a difference is pointed out in the case of *Herzog et al vs. Commissioner*, (C. C. A. 2), decided on January 6, 1941. That case involved federal gift taxes. There the question was whether or not there was a sufficient alienation by the settlor to bring upon him liability for gift taxes. The court held that there was such an alienation and that the decision in the *Hallock* case (*supra*) did not control the issue involved, since in the Herzog case there was not a provision for a reverter as in the *Hallock* case, but the trust instrument provided for a power of termination of the trust timed upon the whim of one of the individual trustees named in the agreement. In that connection the court said:

> "Moreover, as we read the opinion in *Helvering vs. St. Louis Union Trust Company*, 296 U. S. 239, no member of the majority or minority of the court suggested that a discretionary power to terminate a trust which was vested solely in the trustee was sufficient to subject the corpus to an estate tax on the ground that it was part of the property of the grantor. While *Helvering vs. St. Louis Union Trust Company* was overruled by *Helvering vs. Hallock*, 309 U. S. 106, because the contingent reversion retained by the grantor subjected the corpus of the trust to an estate tax, nothing was said about the effect of the discretionary power."

In the instant case the Sixth Circuit Court of Appeals decided against petitioner herein because as it stated:

> "The petitioner contends that inasmuch as his right to acquire the accumulated income of the trust estates depends entirely upon the mere possibility that he shall survive his wife—a circumstance over which he has no control—such mere possibility of his acquiring the accumulated income is no justification for bringing the trusts, with which we are concerned, within the provisions of Section 167 of the Revenue Act of 1932.
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> He urges upon us *Corning vs. Commissioner*, 104 F. 2d 329 (C. C. A. 6), (June 6, 1939), which with respect to 'possibility of reverter' dutifully applied the doctrine of *Helvering vs. St. Louis Trust Company*, 296 U. S. 39. But the *Corning* case is no longer authority upon the subject, for the reason that the Supreme Court in *Helvering vs. Hallock*, 309 U. S. 106 (June 29, 1940) reversing 102 F. 2d 1 (C. C. A. 6), expressely overruled *Helvering vs. St. Louis Trust Company, supra*, and *Becker vs. St. Louis Trust Company*, 296 U. S. 39, as untenable departures from the doctrine of *Klein vs. United States*, 283 U. S. 231, which was distinctly approved."

Thus we submit the Sixth Circuit Court of Appeals in the instant case reversed its decision upon the *Corning* case upon a misapprehension of what the case of *Helver-*

ing vs. Hallock held. The United States Board of Tax Appeals on the other hand refuses to concede that *Helvering vs. Hallock, supra*, has any such interpretation as is placed upon that decision by the Sixth Circuit Court of Appeals in the instant case. In *McLean vs. Commissioner*, 41 B. T. A. 565 (March 8, 1940) the Board said at page 578:

> "The two *St. Louis Union Trust Company* cases cited in the above quotation are no longer to be followed. *Helvering vs. Hallock*, 309 U. S. 106 (January 29, 1940). However, those cases had to do with estate tax, and the *Boeing*, the *Moore* and the present case have to do with income tax. The *St. Louis Union Trust Company* cases were merely referred to and not relied upon in the *Boeing* case; consequently there is no reason why the Board should fail to follow the *Boeing* and the *Moore* cases in the present case."

As an added reason for denying the appeal of petitioner herein the Sixth Circuit Court of Appeals held that the income of the trusts here in question was taxable to settlor (petitioner herein) for the reason that during the joint lives of settlor and his wife (Mary Kaufman Altmaier) they, acting jointly, could terminate the trust at any time. The court interpreted the decision of the Supreme court in *Helvering vs. Clifford*, 309 U. S. 331 (decided February 26, 1940) to mean that where the beneficiary who had "a substantial adverse interest in the disposition of the corpus" was the wife of the settlor, the wife by virtue of her relationship to the settlor is not a person "having a substantial adverse interest" within the meaning of the statute. This interpretation by the Sixth Circuit Court of Appeals of the decision of this court in the case of *Helvering vs. Clifford, supra*, is exactly contrary to the decision by the Circuit Court of Appeals for the First Circuit in the case of *Commissioner vs. Branch*, 114 F. 2d 985 (Oct. 23, 1940). The court in that case in

interpreting the decision of this court in *Helvering vs. Clifford, supra,* said:

> "We do not understand that the case as a general proposition obliterates the separate legal personality of the wife for purposes of determining the gross income of the husband under Section 22 (a)."

In this connection we also direct the attention of the court to the case of *Helvering vs. Wood,* 309 U. S. 344, where this court held that it would not consider the issue as to whether income was taxable under Section 22 (a) of the Revenue Act because that issue was not submitted to the Board of Tax Appeals or to the court below and had been expressly waived by the Commissioner in his brief before the Circuit Court of Appeals. In the instant case such an express waiver and abandonment of the very issue now raised by the Sixth Circuit Court of Appeals is shown by the record (pp. 13 and 14) where the Commissioner in his deficiency notice makes the following statement:

> "The only power to revoke or withdraw the trust in whole or in part was by a joint written instrument by Mrs. O. C. Altmaier and yourself and inasmuch as she holds a substantial beneficial interest in each of the trusts, this provision cannot be made the basis for treating the trusts as being revocable.
>
> In Bureau letter dated October 17, 1935, you were advised that your contention, that under the provisions of Section 166 of the Revenue Act of 1932 the trusts were irrevocable, was conceded. In the same communication, however, you were advised that under the provisions of Section 167 of the same Act it was evident that the income from the trust funds may be taxable to you. * * *
>
> Under the provisions of Section 167 of the Revenue Act of 1932 above cited and the terms of the trust instrument, it is the contention of the Bureau that the income of these trusts may eventually be paid to the settlor of the trusts and for these reasons the Bureau holds the income accruing on them should be taxable to you, the settlor."

In the opening statement by counsel for respondent before the United States Board of Tax Appeals (R. 67) the issue in the case was very definitely narrowed down to the applicability of Section 167 of the Revenue Act of 1932. Petitioner herein therefore holds that when the Circuit Court of Appeals for the Sixth Circuit introduces this issue into the case it violates the rule announced by this court in *Helvering vs. Wood, supra.*

Because of the many conflicts in decisions dealing with the very same subject matter as that involved in the instant case between the Circuit Court of Appeals for the Sixth Circuit and the Circuit Courts of Appeals for other courts above cited and because said Circuit Court of Appeals for the Sixth Circuit has decided an important question of tax law in a way probably untenable because in conflict with the decided weight of authority, including that of this court, it is respectfully submitted that *certiorari* should be granted herein.

Respectfully submitted,

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